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04-599

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

JAY HENDRICKSON, ROSE HENDRICKSON and KATHLEEN O'BRIEN, on behalf of themselves and all others similarly situated,

Petitioners,

—v.—

AMERICAN SKANDIA LIFE ASSURANCE CORPORATION, AMERICAN SKANDIA MARKETING, INCORPORATED, AMERICAN SKANDIA INVESTMENT HOLDING CORPORATION, ABC CORP., INC. 1 through ABC CORP., INC. 99, and LMN CORP., INC. 1 through LMN CORP., INC. 99,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

RESPONDENTS' BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

I. Whether the United States Court of Appeals for the Second Circuit correctly found that an issuer of a variable annuities prospectus did not violate federal securities laws by failing to include in the prospectus non-mandatory language suggested in an NASD Notice To Members directed to registered representatives at the point of sale rather than the issuer of the security.

II. Whether the Second Circuit contravened this Court's precedent when it failed to consider a joint report issued by SEC staff and the NASD that was not published until after the Second Circuit's decision and, in any event, was addressed to registered representatives and did not represent the opinion of the SEC itself.

III. Whether the Second Circuit contravened this Court's precedent when it found that, as a matter of law, the variable annuities prospectus contained no material omissions because the alleged omissions did not significantly alter the total mix of information available to the investor.

RULE 14.1(B) STATEMENT

Petitioners "List of All Parties" (Pet. at iii) is accurate.

RULE 29.6 STATEMENT

Pursuant to Supreme Court Rule 29.6, Defendants-Respondents state that American Skandia Life Assurance Corporation and American Skandia Marketing, Inc. are wholly owned by American Skandia, Inc., a non-public company. American Skandia Investment Holding Corporation is the former name of American Skandia, Inc. American Skandia, Inc., is wholly owned by Skandia U.S. Inc., a non-public company. Skandia U.S. Inc. is wholly owned by Prudential Financial, Inc., a public company.

TABLE OF CONTENTS

	PAGE
QUESTIONS PRESENTED	i
RULE 14.1(B) STATEMENT	ii
RULE 29.6 STATEMENT	ii
TABLE OF CONTENTS	iii
TABLE OF AUTHORITIES	iv
STATEMENT OF THE CASE	1
REASONS FOR DENYING THE WRIT	3
I. The Petition Presents No Important Question Of Federal Law	5
II. The Decision Of The Second Circuit Did Not Contravene Supreme Court Precedent	13
A. The Second Circuit Court Of Appeals Did Not Contravene Supreme Court Precedent When It Did Not Give Judicial Deference To A Joint SEC/NASD Report	13
B. The Second Circuit Court of Appeals Did Not Contravene Supreme Court Precedent When It Dismissed the Complaint	17
CONCLUSION	20

TABLE OF AUTHORITIES

Cases: PAGE

Air Brake Sys., Inc. v. Mineta, 357 F.3d 632 (6th Cir. 2004) 14

Alaska Dep't of Envtl. Conservation v. Envtl. Prot. Agency, 540 U.S. 461 (2004) 14

Basic, Inc. v. Levinson, 485 U.S. 224 (1988) 18

Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837 (1984) 12, 14

Christensen v. Harris County, 529 U.S. 576 (2000) 12, 14, 15

Clackamas Gastroenterology Assocs., P.C. v. Wells, 538 U.S. 440 (2003) 14

Desiderio v. NASD, Inc., 191 F.3d 198 (2d Cir. 1999), *cert. denied*, 531 U.S. 1069 (2001) 11

Drnek v. Variable Annuity Life Ins. Co., No. CIV 01-242-TUC-WDB, 2004 WL 1098919 (D. Ariz. May 4, 2004).. 10

Echeverria v. Chicago Title & Trust Co., 256 F.3d 623 (7th Cir. 2001) 14

Ganino v. Citizens Utils. Co., 228 F.3d 154 (2d Cir. 2000) 15, 18

Johnson v. Aegon USA, Inc., C.A. No. 1:01-CV-2617-CAP, 2004 U.S. Dist. LEXIS 20471 (N.D. Ga. Sept. 20, 2004) 11

PAGE

Klitzman v. Bache Halsey Stuart Shields, Inc., 499 F. Supp. 255 (S.D.N.Y. 1980) 12

NASD Dep't of Enforcement v. Am. Express Fin. Advisors Inc., No. CAF020057, NASD Letter of Acceptance, Waiver & Consent (Nov. 12, 2002) 10

NASD Dep't of Enforcement v. Am. United Life Ins. Co., No. C05010011, NASD Regulation, Inc. Office of Hearing Officers, Order Accepting Offer of Settlement (2002) 11

In re NBTY, Inc., Sec. Litig., 224 F. Supp.2d 482 (E.D.N.Y. 2002) 18

Nelson v. Pac. Life Ins. Co., No. Civ. A. CV 203-131, 2004 WL 1592617 (S.D. Ga. July 12, 2004) 10

Perez-Gonzales v. Ashcroft, 379 F.3d 783 (9th Cir. 2004) 14

SEC v. Geon Indus., Inc., 531 F.2d 39 (2d Cir. 1976) 6

Stevelman v. Alias Research Inc., 174 F.3d 79 (2d Cir. 1999) 6

TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438 (1976) 17

In re Ultimate Corp. Sec. Litig., No. 85 CIV. 5944 (CSH), 1989 WL 79372 (S.D.N.Y. July 11, 1989) 18

United States v. Mead Corp., 533 U.S. 218 (2001) 12

PAGE

STATUTES AND RULES

Code of Federal Regulations,
17 C.F.R. § 240.10b-5 ..... 1, 14

NASD Conduct Rule IM-2310 7

NASD Notice to Members 99-35
(May 1999) .....*passim*

Second Circuit Local Rule 23 19

Securities Act of 1933, 15 U.S.C. §§ 77(k),
77(l) & 77(o) 1, 12

Securities Exchange Act of 1934,
15 U.S.C. §§ 78j(b), 78t(a), 78o-3(a)
& 78w(a)..... 1, 14

Supreme Court Rule 10(c)..... 3, 5

PAGE

OTHER AUTHORITIES

Joint SEC/NASD Report on Examination Findings Regarding Broker-Dealer Sales of Variable Insurance Products (June 2004) (available at *http://www.sec.gov/news/studies/secnasdvip.pdf*) 13, 15, 16

NASD News Release *"NASD Proposes Specific Requirements for Deferred Variable Annuity Sales, Concern Over Suitability, Disclosure, Supervision Cited"* (Apr. 2004) (available at *http://www.nasd.com/stellent/idcplg?IdcService=SS_GET_PAGE&ssDocName=NASDW_002835&ssSourceNodeId=553.)* 16

NASD Respondent's Brief in Opposition On Petition for Writ of Certiorari in Desiderio v. NASD, Inc., Case No. 99-1285, 1999 WL 33640362 (U.S. 1999) 11

SEC Release No. 34-36383 *"Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Application of the Rules of Fair Practice to Transactions in Exempted Securities and an Interpretation of its Suitability Rule,"* 1995 WL 625609, 4-5 (S.E.C. Release No. 34-36383, Oct. 17, 1995) 7

STATEMENT OF THE CASE

Respondents are American Skandia Life Assurance Corporation ("ASLAC"), American Skandia Marketing, Inc. ("ASM") and American Skandia Investment Holding Corporation ("ASICH") (now known as American Skandia, Inc.) (collectively "American Skandia"). American Skandia issues and distributes variable annuities.

Petitioners are individuals who in early 2000 purchased American Skandia tax-deferred variable annuities —not from American Skandia—but from an independent broker-dealer, World Marketing Alliance, Inc. ("WMA"), and used the variable annuities to fund their tax-deferred qualified retirement plans. WMA is not a party to this action.

Petitioners allege that the American Skandia variable annuities prospectuses and other unspecified documents contained misstatements and omissions of material fact, in violation of Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act"), as amended, 15 U.S.C. §§ 78j(b) and 78t(a), and Rule 10b-5 promulgated thereunder, 17 C.F.R. §240.10b-5; and Sections 11 and 12(a)(2) of the Securities Act of 1933 ("Securities Act"), 15 U.S.C. §§ 77(k), 77(l) and 77(o). The District Court and a unanimous panel of the Second Circuit, however, held that Petitioners failed to meet the threshold requirement of pleading facts establishing that American Skandia made an untrue statement of material fact or made a material omission. Rather than accept these unequivocal and damning rejections of their argument, Petitioners seek this Court's review.

This action improperly attempts to litigate literally thousands of individual suitability determinations on a class-wide basis against American Skandia. However, American Skandia was only the issuer of the securities.

It was not responsible for—and did not make—those suitability determinations at the point of sale.

Petitioners' argument is twofold. First, they contend that the American Skandia's variable annuities prospectuses contained material misstatements in the form of categorical recommendations that Petitioners should purchase variable annuities to fund their qualified retirement plans. Petitioners argue that using a variable annuity to fund a qualified retirement plan is "virtually never suitable." (Pet. at 6.) The prospectuses, however, clearly do not make any such recommendation. Second, Petitioners contend that American Skandia's variable annuities prospectuses omitted certain language allegedly mandated by the National Association of Securities Dealers ("NASD") Notice to Members 99-35 (the "Notice" or "NTM 99-35"). (Pet. at 6.) However, the NASD Notice merely sets forth guidelines for registered representatives at the point of sale and creates no duty to disclose such material in American Skandia's prospectuses.

Petitioners' claim relies on a misleading partial quote of NTM 99-35, issued by the NASD in May of 1999. Petitioners allege that NTM 99-35 dictates that it is "never" suitable to fund a qualified retirement plan with a tax-deferred variable annuity because the qualified retirement plan is itself tax-deferred. The Notice itself refutes this central premise of Petitioners' claim. In fact, NTM 99-35 specifically states that while it provides guidelines, *they are not mandatory*. Additionally, NTM 99-35 suggests only that the registered representative of NASD broker-dealers should not recommend the use of a variable annuity in a qualified retirement plan unless its other features support the recommendation. A variable annuity combines many important features having nothing to do with the tax treatment of investment gains

(*e.g.*, a guaranteed stream of payments, highly flexible investment options and family protection through the death benefit)—features unavailable in alternative investment vehicles. Both Judge Pollack and a unanimous panel of the Second Circuit correctly recognized the false conflict between a statement American Skandia did not make, and a conclusion the NASD never reached.

Moreover, the Notice is directed to NASD broker-dealers supervising registered representatives—the very persons who, acting at the point of sale with the individual investor, are charged with making the individualized, multi-factor suitability analysis called for by the NASD's "know your customer" rule invoked by Petitioners. The Notice is *not* directed to, or binding on, variable annuities issuers responsible for the disclosure in prospectuses.

Both the District Court and the Second Circuit correctly concluded that the American Skandia variable annuities prospectuses contained no material misstatements, and fully and fairly disclosed all required material facts. These defects in Petitioners' claim could not be remedied by an amendment to the complaint, and therefore the District Court and the Second Circuit properly dismissed the action with prejudice.

REASONS FOR DENYING THE WRIT

The Petition fails to satisfy any of the criteria for a grant of certiorari. Supreme Court Rule 10(c). First, Petitioners have pointed to no important question of federal law that this Court should resolve. Petitioners' argument that NASD Rules deserve some level of judicial deference has no relevance in a case such as this one where there is no NASD Rule (or even Securities and Exchange Commission ("SEC") Rule) at issue. Peti-

tioners fundamentally mischaracterize this case. This case is about whether an issuer of a prospectus violated federal securities laws when it did not include within the prospectus non-mandatory language suggested by the NASD directed, not towards the issuer, but towards registered representatives responsible for the suitability determinations at the point of sale. Both the District Court and the Second Circuit, after painstakingly reviewing the prospectus at issue, correctly found that it did not contain any material misrepresentations or omissions.

Despite Petitioners' contention to the contrary, the Second Circuit considered and specifically found that NASD NTM 99-35 did not apply to the issuer of the prospectus. Relying on the plain language of NTM 99-35, the Second Circuit found it only applied to registered representatives making recommendations at the point of sale. Petitioners' reliance on three district court cases to demonstrate discordance among courts is unavailing and meritless, as these cases are factually distinguishable. Therefore, the issue of judicial deference to NASD Rules is nothing more than a red herring. However, were this Court to consider the issue, the NASD Notice is not deserving of judicial deference.

Second, the decisions below are consistent with this Court's precedent. Petitioners assert that the Second Circuit contravened this Court's precedent when it failed to give judicial deference to a June 2004 report issued jointly by SEC staff and the NASD. (Pet. at 25-27.) It must be noted that the Report was not published until several weeks after the Second Circuit's May 14, 2004 decision. Moreover, it is well-settled that letters or reports, which do not express the opinion of an executive or administrative agency, do not merit judicial deference. Additionally, Petitioners assert that the Second

Circuit's decision went against this Court's jurisprudence by deciding the issue of materiality as a matter of law, as opposed to allowing the trier of fact make this determination. (Pet. at 27-29.) However, here again it is well established that a court may determine materiality as a matter of law if, as here, the information allegedly omitted does not alter the total mix of information available to an investor.

Finally, even if the lower courts reached an erroneous decision below, this is insufficient to warrant this Court's review. The unanimous, but unpublished opinion of the Second Circuit has no binding or precedential effect.

In sum, the Petition fails to satisfy any of the criteria of Supreme Court Rule 10(c) meriting this Court's review. As such, the Petition for Certiorari should be denied.

I. THE PETITION PRESENTS NO IMPORTANT QUESTION OF FEDERAL LAW

This case presents no important question of federal law that this Court should address. Petitioners' argument that NASD Rules deserve some level of judicial deference mischaracterizes the facts of this case, and is nothing more than a red herring because this case is not about an NASD Rule (or even an SEC Rule, for that matter). The issue in this case is whether the prospectuses issued by American Skandia violated federal securities laws by failing to include language suggested in NASD NTM 99-35.[1]

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[1] Petitioners contend that American Skandia implicitly admitted an NASD violation when it changed the wording of its prospectuses in October of 2000 (Pet. at 7 n.2). This argument is meritless. It is well-established that a revised disclosure does not necessarily render a previous statement or disclosure inadequate or fraudulent. *See*

The District Court, per Judge Milton Pollack, and the Second Circuit fully considered and correctly decided the issues in this case. Judge Pollack thoroughly reviewed the prospectuses at issue, and found that the prospectuses correctly and adequately disclosed the tax nature of variable annuities and of qualified retirement plans. Judge Pollack carefully reviewed the prospectuses, and determined that they contained neither material misstatements nor omissions. Specifically, he found:

> Although the Prospectuses undeniably indicate that a variable annuity may be used as an investment vehicle for a qualified retirement plan, it is not true, as Plaintiffs state, that this is never appropriate. NASD Notice 99-35 itself states that a *registered representative* may recommend a variable annuity for a tax-qualified retirement account "when its other benefits, such as lifetime income payments, family protection through the death benefit, and guaranteed fees" support the recommendation. (Pet. App. B at 10a. (emphasis added).)

The Second Circuit unanimously concurred with Judge Pollack's analysis and decision. "As the district court correctly observed, neither NASD Notice 99-35 nor SEC Form N-4 imposes a duty on defendants to include in its prospectuses the warning sought by plaintiffs" (Pet. App. A at 5a.) These decisions are correct in light of the plain language of the NASD Notice.

In May of 1999, the NASD issued NTM 99-35 which "focuse[d] on deferred variable annuity sales and provide[d] a set of guidelines that [were] intended to assist members in developing appropriate procedures relating to variable annuity *sales to customers*." (Pet. App. E at

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SEC v. Geon Indus., Inc., 531 F.2d 39, 52 (2d Cir. 1976); *Stevelman v. Alias Research Inc.*, 174 F.3d 79, 84 (2d Cir. 1999).

18a (emphasis added).) The plain language of the Notice states that "the specific procedures described *are not mandatory*." (*Id.* (emphasis added).) NASD NTM 99-35 relates to NASD Conduct Rule 2310, (*i.e.*, the Suitability Rule).[2] (Pet. App. E 21a - 22a.) The Suitability Rule explains the obligation to determine whether an investment is "suitable" for a particular investor, which is an inherently individualized inquiry. *See* NASD Conduct Rule IM-2310. It requires the registered representative (*i.e.*, the broker) to consider the investor's wants, needs, risk tolerance and financial situation, amongst other factors. *See SEC Release No. 34-36383 "Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Application of the Rules of Fair Practice to Transactions in Exempted Securities and an Interpretation of its Suitability Rule*," 1995 WL 625609, at *4-5 (S.E.C. Release No. 34-36383, Oct. 17, 1995) (stating that the two most important considerations in a suitability determination are "the customer's capability to evaluate investment risk independently, and the extent to

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[2] NASD Conduct Rule 2310 states:

(a) In recommending to a customer the purchase, sale or exchange of any security, a member shall have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts, if any, disclosed by such customer as to his other security holdings and as to his financial situation and needs.

(b) Prior to the execution of a transaction recommended to a non-institutional customer . . . a member shall make reasonable efforts to obtain information concerning:

(i) the customer's financial status;
(ii) the customer's tax status;
(iii) the customer's investment objectives; and
(iv) such other information used or considered to be reasonable by such member or registered representative in making recommendations to the customer.

which the customer intends to exercise independent judgment in evaluating a member's recommendation"). This obligation is imposed on the broker's registered representative at the point of sale (*i.e.*, the point at which the investor—and his or her individual investment criteria—can be identified and considered).

Within the framework of the Suitability Rule, the NASD Notice specifically states:

> When a *registered representative recommends* the purchase of a variable annuity for any tax-qualified retirement account (*e.g.*, 401(k) plan, IRA), the *registered representative* should disclose to the customer that the tax deferred accrual feature is provided by the tax-qualified retirement plan and that the tax deferred accrual feature of the variable annuity is unnecessary. The *registered representative* should *recommend* a variable annuity only when its other benefits, such as lifetime income payments, family protection through the death benefit, and guaranteed fees, support the recommendation. (Pet. App. E at 25a (emphasis added).)

Therefore, the plain language of NASD NTM 99-35 only applies to registered representatives recommending the variable annuity.

The Second Circuit considered the plain language of NASD NTM 99-35, and specifically found that it did not apply to this case:

> As the district court correctly observed, neither NASD Notice 99-35 nor SEC Form N-4 imposes a duty on defendants to include in its prospectuses the warning sought by plaintiffs. By its terms, NASD Notice 99-35 applies only to *registered representatives* recommending the pur-

> chase of a variable annuity; it does not require annuity issuers to include a warning in a prospectus or other offering documents. (Pet. App. A at 4a. (emphasis added).)

Thus, the Second Circuit held that NTM 99-35 did not apply to American Skandia, but only to the registered representatives working at the point of sale. Notwithstanding, the Second Circuit further considered the relevance of NASD NTM 99-35, and found that it did not apply because the prospectuses did not recommend the purchase of the variable annuities:

> Even if the [NASD] Notice did apply to issuers, the prospectus challenged in this case *does not recommend the purchase of annuities*; it says only that annuities "may be a suitable" investment. Indeed, the prospectus specifically advises prospective investors to seek professional tax advice before purchasing annuities for use in a qualified plan. Prospectus at 41. (Pet. App. at 4a-5a (emphasis added).)

As Petitioners concede, and as Judge Pollack correctly found, American Skandia did not recommend that Petitioners purchase variable annuities for their retirement accounts. This determination was made by an independent broker-dealer, who Petitioners did not name as a defendant in this action. As Judge Pollack noted: "Plaintiffs are not, however, bringing any charges against the broker from whom they purchased the variable annuity." (Pet. App. B at 9a.)

Despite the plain language of NASD NTM 99-35, Petitioners argue that every other court that has decided the issue has disagreed with the Second Circuit. (Pet. 13-14.) Petitioners cite to three district court cases in support of their argument. These cases, however, do not warrant this Court's review for two reasons.

First, alleged conflict between a court of appeals and district court opinions are insufficient to warrant this Court's review. Uniformity in federal matters is achieved when this Court reviews various court decisions that are otherwise final in the absence of Supreme Court review. This is not the case.

Second, there is no conflict because the three district court cases are factually distinguishable from this case. In two of the cases, the courts found that the issuer was, in effect, acting as the registered representative—thus falling within the purview of NASD NTM 99-35. In *Drnek v. Variable Annuity Life Ins. Co.*, No. CIV 01-242-TUC-WDB, 2004 WL 1098919, at *3 (D. Ariz. May 4, 2004), the district court denied defendants' motion to dismiss, finding that because defendants sold the variable annuity directly to plaintiffs, this created a "relationship of trust between buyers and sellers . . . which would create a duty to inform the buyers" of the information contained in the NASD Notice. Similarly, in *Nelson v. Pac. Life Ins. Co.*, No. Civ. A. CV 203-131, 2004 WL 1592617, at *4 (S.D. Ga. July 12, 2004), the district court denied defendants' motion to dismiss, highlighting that plaintiffs alleged a principal-agency relationship with the registered representative who sold the variable annuity to plaintiffs. Petitioners have not alleged a principal-agency relationship between American Skandia and the registered representative who sold them the variable annuities at issue; in fact, they are unable to do so because Petitioners did not purchase the variable annuities in question from American Skandia, but from an independent broker-dealer.[3]

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[3] This same principle distinguishes the NASD enforcement cases upon which Petitioner seek to rely. *See NASD Dep't of Enforcement v. Am. Express Fin. Advisors, Inc.*, No. CAF020057, NASD Letter of Acceptance, Waiver and Consent (Nov. 12, 2002) (finding

Finally, in *Johnson v. Aegon USA, Inc.*, C.A. No. 1:01-CV-2617-CAP, 2004 U.S. Dist. LEXIS 20471 (N.D. Ga. Sept. 20, 2004), the district court made a factual determination regarding the disclosure in a prospectus different from the one at issue here. Petitioners have not provided any evidence that there is any similarity between American Skandia's prospectuses and those at issue in *Johnson*. The fact that the district court in *Johnson* denied defendants' motion to dismiss after reviewing a different prospectus does not conflict with the Second Circuit's opinion. That three district court opinions, interpreting different prospectuses and under different factual circumstances, reached different conclusions than the Second Circuit, does not call the Second Circuit's opinion into question.

In arguing that NASD Rules deserve judicial deference Petitioners mischaracterize this case, because there is no NASD Rule at issue. Here, the document at issue is simply an NASD Notice to Members, which the NASD recognizes is not mandatory.

An NASD Notice to Members, which only suggests guidelines, does not deserve judicial deference. In its own words, the NASD is a private not-for-profit corporation chartered in Delaware. *See NASD Respondent's Brief in Opposition On Petition for Writ of Certiorari in Desiderio v. NASD, Inc.*, Case No. 99-1285, 1999 WL 33640362, at *2 (U.S.); *see also Desiderio v. NASD, Inc.*, 191 F.3d 198, 206 (2d Cir. 1999), *cert. denied*, 531 U.S. 1069 (2001) (holding the NASD is a private—not

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registered representative violated NASD Conduct Rules in enforcement action arising out of registered representative's failure to make certain oral disclosures at the point of sale); *NASD Dep't of Enforcement v. Am. United Life Ins. Co.*, No. C05010011, NASD Regulation, Inc. Office of Hearing Offices, Order Accepting Offer of Settlement (2002) (same).

state—actor). Although it is registered with the SEC as a self-regulatory organization pursuant to 15 U.S.C. § 78o-3(a), it was not created by statute. *Id.* Neither its directors nor its executives are governmental officials or appointees. *Id.* It receives no funding from any government, federal or state. *Id.* It has the power to govern the conduct of its members by virtue of the contractual relationship between it and its members. *Klitzman v. Bache Halsey Stuart Shields Inc.*, 499 F. Supp. 255, n.1 (S.D.N.Y. 1980). As such, neither NASD Rules nor Notices are binding on parties that are not NASD members.

As defined by this Court, judicial deference is due to a governmental agency where there is an express congressional authorization to engage in rulemaking or adjudication process that produces a rule or regulation. *Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837 (1984). This is known as *Chevron* deference. This Court has also extended a lower standard of deference to a governmental agency's interpretations of its own rules. *United States v. Mead Corp.*, 533 U.S. 218 (2001). This is referred to as *Skidmore* deference. However, this Court has specifically found that interpretations contained in opinion letters, and particularly those that were not arrived at after a formal adjudication or notice-and-comment rulemaking process, do not deserve judicial deference. *Christensen v. Harris County*, 529 U.S. 576, 587 (2000). No court, however, has extended any level of judicial deference to non-mandatory suggestions of a private corporation, such as the NASD.

Petitioners' assertion that an NASD Rule deserves judicial deference is nothing more than an academic argument. In this case, the idea that an NASD Notice to Members, which has no effect on non-members, should carry the force of law is meritless, and does not deserve

this Court's attention. As such, Petitioners have failed to raise an important question of federal law that this Court should address.

II. THE DECISION OF THE SECOND CIRCUIT DID NOT CONTRAVENE SUPREME COURT PRECEDENT

A. The Second Circuit Court Of Appeals Did Not Contravene Supreme Court Precedent When It Did Not Give Judicial Deference To A Joint SEC/NASD Report

In a last ditch effort to revive their losing cause, Petitioners implored the Second Circuit to consider a joint report issued by SEC staff and the NASD entitled "Joint SEC/NASD Report on Examination Findings Regarding Broker-Dealer Sales of Variable Insurance Product" ("Report"). *See* Office of Compliance Inspection and Examinations, United States Securities and Exchange Commission/NASD "*Joint SEC/NASD Report on Examination Findings Regarding Broker-Dealer Sales of Variable Insurance Product*" (available at *http://www.sec.gov/news/studies/secnasdvip.pdf*). Petitioners argue that by failing to give the Report judicial deference, the Second Circuit contravened this Court's precedent. (Pet. at 26-27.) However, Petitioners' argument is unavailing for three reasons. First, the Report was not issued until June 9, 2004—almost four years after the class period and some three weeks after the Second Circuit's decision.[4] Second, a report that explicitly does not

[4] On May 14, 2004, the Second Circuit issued its unpublished opinion. On May 28, 2004, Petitioners filed a Petition for Rehearing and Petition for Rehearing *En Banc*. Subsequently, on July 15, 2004, Petitioners filed a letter with the Clerk of Court for the Second Circuit asking the panel take into consideration the Report in question. The Petition for Rehearing was denied on July 30, 2004. Therefore,

represent the views of the SEC is not entitled to judicial deference. And third, contrary to Petitioners' contention, the Report does not support their position.

American Skandia does not dispute the fact that rules promulgated by the SEC pursuant to its rulemaking authority carry with it the force of law, *i.e.*, *Chevron* deference. Rule 10b-5, which is promulgated under 15 U.S.C. § 78w(a), is a prime example of such a rule deserving judicial deference. However, as this Court has clearly held, interpretations, such as opinion letters, "which are not the result of a formal adjudication or notice-and-comment process," lack the force of law, and therefore are not necessarily accorded judicial deference. *Christensen*, 529 U.S. at 587; *see also Alaska Dep't of Envtl. Conservation v. Envtl. Prot. Agency*, 540 U.S. 461, 487 (2004) (holding that an agency's interpretation contained in an internal guidance manual does not deserve judicial deference); *Clackamas Gastroenterology Assocs., P.C. v. Wells*, 538 U.S. 440, 449 n.9 (2003) (holding that the EEOC's compliance manuals are not controlling); *Perez-Gonzales v. Ashcroft*, 379 F.3d 783, 793-96 (9th Cir. 2004) (finding that agency interpretation contained in a guidance memorandum that conflicted with immigration statutes did not deserve deference); *Air Brake Sys., Inc. v. Mineta*, 357 F.3d 632, 642-43 (6th Cir. 2004) (finding that the opinion letters of the chief counsel of the NHTSA are too informal to merit judicial deference); *Echeverria v. Chicago Title & Trust Co.*, 256 F.3d 623, 630 (7th Cir. 2001) (holding that judicial deference is not due to "unofficial interpretations which the agency itself does not view as bind-

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it was impossible for the Second Circuit panel that originally decided the case to have disregarded a report that did not exist. Moreover, as discussed *infra*, the Second Circuit in deciding a Petition for Rehearing was not obligated to rely on a report which does not represent the views of the SEC.

ing"); *Ganino v. Citizens Utils. Co.*, 228 F.3d 154, 163 (2d Cir. 2000) (holding that, unlike an SEC rule promulgated pursuant to its rulemaking authority, an SEC Staff Accounting Bulletin, "does not carry with it the force of law").

The Report specifically states that "[t]his report represents the findings of the Staff of the Commission and NASD, and *not the Commission itself*." Report at 3 n.1 (emphasis added). There is no basis to argue that a report by the staff, not adopted by the SEC, carries with it the same force of law as, for example, Rule 10b-5. In the words of this Court, it is a summary of findings, "not one arrived at after, for example a formal adjudication or notice-and-comment rulemaking. Interpretations such as those in opinion letters, like interpretations contained in policy statements, agency manuals, and enforcement guidelines, all of which lack the force of law—do not warrant *Chevron*-style deference." *Christensen*, 529 U.S. at 587 (internal citation omitted). As such, this Report does not merit judicial deference.

Moreover, Petitioners mischaracterize the content and import of the Report. This Report does not mandate that issuers of variable annuities prospectuses include any specific language within their prospectus. The Report "is not a comprehensive roadmap for compliance and supervision with respect to the sale of variable insurance products, but rather points out examples of common problems that may be encountered, and some measures that firms are using to ensure better compliance." Report at 3. The section Petitioners quote from is entitled "Disclosure" and states:

> With regards to sales of annuities in tax-qualified plans, the NASD states that when a *registered representative* recommends the purchase of a variable annuity for any tax-qualified retire-

> ment account (*e.g.*, 401(k) plan, IRA), the *registered representative* should disclose to the customer that the tax-deferred accrual feature is provided by the tax-qualified retirement plan and that the tax-deferred accrual feature of the variable annuity is unnecessary. Report at 18 (emphasis added).

Notwithstanding Petitioners' implication to the contrary, the Report does not state that an issuer of a variable annuities prospectus is mandated to include any language within its prospectus. The Report simply states that registered representatives *should*—not must—inform their customers that it is unnecessary to purchase a variable annuity for its tax-deferred feature for a tax-qualified retirement plan. This is a far cry from mandating the issuer of the prospectus to set forth this language in a prospectus that goes to all potential investors irrespective of their individual investment concerns.[5]

Petitioners' argument that this Report deserves judicial deference is not in accord with Supreme Court precedent, and is not supported by the Report itself. As such, Petitioners' claim that the Second Circuit's opinion contravenes this Court's precedent is meritless.

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[5] Further detracting from Petitioners' argument is the fact that the NASD is in the process of proposing a new rule regarding variable annuity sales. *See* April 26, 2004 NASD News Release "NASD Proposes Specific Requirements for Deferred Variable Annuity Sales, Concern Over Suitability, Disclosure, Supervision Cited" (available at *http://www.nasd.com/stellent/idcplg?IdcService=SS_GET_PAGE&ssDocName=NASDW_002835&ssSourceNodeId=553*). This release highlights the key requirements of the proposed rule. Most tellingly, there is absolutely no mention of any duty imposed on issuers of variable annuities prospectuses. The proposed rule focuses exclusively on registered representatives.

B. The Second Circuit Court of Appeals Did Not Contravene Supreme Court Precedent When It Dismissed the Complaint

As previously noted, both Judge Pollack and a unanimous panel of the Second Circuit found that the American Skandia prospectuses did not contain any material omissions. Petitioners contend that the Second Circuit's decision contravened this Court's precedent by determining materiality as a matter of law, as opposed to allowing the issue to go to the trier of fact. (Pet. at 27.) However, as this Court has recognized time and again, materiality can be determined as a matter of law if the alleged omission is obviously unimportant in light of the disclosures made. Moreover, even if the factual determination of the Second Circuit was incorrect, this unpublished decision is not enough to merit this Court's review.

It is well established by this Court that an "omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding" how to act. *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976). Stated another way: "there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." *Id.*

It is equally well-settled that "only if the established omissions are 'so obviously important to an investor, that reasonable minds cannot differ on the question of materiality' is the ultimate issue of materiality appropriately resolved 'as a matter of law' . . . ." *Id.* at 450.

After carefully reviewing the prospectuses, Judge Pollack aptly concluded:

> Nor do the allegedly omitted facts significantly alter the total mix of information made available. The Prospectuses clearly state that *both variable annuities and tax qualified retirement plans are tax deferrable*. That is enough to alert all reasonable investors to the fact that it is unnecessary, if solely for tax reasons, to use a variable annuity to fund a tax-deferred retirement account. *See In re NBTY, Inc., Sec. Litig.*, 224 F. Supp.2d 482, 495 (E.D.N.Y. 2002); *In re Ultimate Corp. Sec. Litig.*, No. 85 CIV. 5944 (CSH), 1989 WL 79372, at *5 (S.D.N.Y. July 11, 1989) ("Liability does not arise from the failure to disclose that which should be obvious to the average investor."). The other benefits of the variable annuities are also clearly set forth, as well as the fee structure for purchase of the annuity.
>
> The disclosures in the Prospectuses, taken in context, conclusively disprove the materiality of the alleged omissions and are thus fatal to the Plaintiffs' claims. (Pet. App. B at 10a-11a. (emphasis in original).)

The Second Circuit conducted a *de novo* review of the record and the prospectuses at issue, and likewise concluded that the American Skandia prospectuses contained no material omission:

> Nor did the failure to include the warning sought by plaintiffs constitute a material omission. An omission is material if there is a "substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the total mix of information made available." *Basic, Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988); *accord Ganino v. Citizens Utils. Co.*, 228 F.3d 161-62.

> Here the prospectus clearly states that the investment gains on annuities are not taxable "until an amount is received (a 'distribution')," Prospectus at 39, and that contributions to qualified retirement plans are "not taxable until distributions are made," Prospectus at 42. From this information, the reasonable investor would know that, since taxes on qualified retirement plans are not assessed until a distribution is made, funding a replacement fund with deferred annuities would provide no additional tax advantage. Adding a warning stating that the tax-deferred feature of a deferred annuity is "unnecessary" when the annuity is to fund a qualified retirement plan investments thus would not have "significantly altered the total mix of information" in the prospectus. (Pet. App. A at 5a-6a.)

Both Judge Pollack and the Second Circuit independently reviewed the prospectuses with painstaking care and correctly decided that the alleged omission was not material as a matter of law. These factual determinations do not contravene this Court's precedents.

Even if, *arguendo*, the Second Circuit did erroneously decide this case, it is still insufficient to warrant review by this Court. The Second Circuit's unanimous decision was an unpublished summary order. Pursuant to Second Circuit Local Rule 23, unpublished opinions cannot be cited as precedential authority to any court, including to the Second Circuit. *See* United State Court of Appeals for the Second Circuit, Local Rule 23 (available at http://www.ca2.uscourts.gov/). In other words, the decision of the Second Circuit has no binding effect on any court. Thus, if confronted with a factually similar case, the Second Circuit could reach a different decision.

The Second Circuit made a complex factual determination based on the specific facts of this case; it did not conflict with this Court's jurisprudence. Petitioners' argument to the contrary is unavailing.

CONCLUSION

For the reasons set forth above, the Petition for a Writ of Certiorari should be denied.

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